Supreme Court, U.S.
FILED
JAN 21
CLERK

No. 99-742

IN THE
Supreme Court of the United States

ALBERT AND ESTELLE BINDER, in their individual capacities and on behalf of all persons similarly situated,

Petitioners,

v.

IAN R. WILSON, CARY S. FITCHEY, MARK L. STEVENS and DELOITTE & TOUCHE LLP,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF IN OPPOSITION FOR RESPONDENT DELOITTE & TOUCHE LLP

LOIS D. THOMPSON
Counsel of Record
DONALD S. URRABAZO
PROSKAUER ROSE LLP
Attorneys for Respondent Deloitte & Touche LLP
2049 Century Park East
Los Angeles, CA 90067
(310) 557-2900

157388
Counsel Press LLC
(800) 274-3321 • (800) 359-6859

BEST AVAILABLE COPY

STATEMENT PURSUANT TO RULE 29.6

Rule 29.6 of the Rules of This Court does not apply to Respondent Deloitte & Touche LLP because it is a limited liability partnership and not a nongovernmental corporation.

TABLE OF CONTENTS

	Page
Statement Pursuant to Rule 29.6	i
Table of Contents	ii
Table of Cited Authorities	iv
Preliminary Statement	1
Statement of the Case	2
I. Objection to Petition	2
II. The Facts Pertinent to Deloitte	3
Reasons for Denying the Writ	8
I. The Ninth Circuit Correctly Concluded That A Presumption Of Reliance Does Not Apply in This Case.	8
II. The Ninth Circuit Correctly Held That This Case Does Not Primarily Involve Omissions And, Therefore, the *Affiliated Ute* Presumption Does Not Apply	11
III. The Binder Decision Presents No Questions of National Importance That The Supreme Court Must Settle	12
IV. *Basic* Did Not Alter the *Affiliated Ute* Presumption	15

Contents

	Page
V. The Ninth Circuit Correctly Concluded That the Putative Class Could Not Invoke a Presumption of Reliance on the OTC Market for AVBC Stock	16
VI. Petitioner Failed to Establish a Genuine Issue of Fact with Respect to the Demonstrated Inefficiency of the OTC Market for AVBC Stock	19
VII. The Record Established That Deloitte's Alleged Misrepresentations and Omissions Did Not Cause Petitioner's Loss	21
VIII. The Decision to Decertify the Class Does Not Conflict With Supreme Court Precedent	22
Conclusion	26

TABLE OF CITED AUTHORITIES

Page

Cases:

Affiliated Ute Citizens of Utah v. United States, 406 U.S. 128 (1972) ..... *passim*

Basic v. Levinson, 485 U.S. 224 (1988) 9, 10, 15, 16, 17, 18, 19, 20, 21

Binder v. Gillespie, 184 F.3d 1059 (9th Cir. 1999) .. 1

Blackie v. Barrack, 524 F.2d 891 (9th Cir. 1975), *cert. denied*, 429 U.S. 816 (1976) 9, 10

Cammer v. Bloom, 711 F. Supp. 1264 (D.N.J. 1989) 18, 19

Cavalier Carpets, Inc. v. Caylor, 746 F.2d 749 (11th Cir. 1984) 13, 14

East Texas Motor Freight System, Inc. v. Rodriguez, 431 U.S. 395 (1977) 25

Finkel v. Docutel/Olivetti Corporation, 817 F.2d 356 (5th Cir. 1987), *cert. denied*, 485 U.S. 959 (1988) 13, 14, 15

General Telephone Co. of Southwest v. Falcon, 457 U.S. 147 (1982) 24, 25

Cited Authorities

Page

Huddleston v. Herman & MacLean, 640 F.2d 534 (1981), *aff'd in part and rev'd in part on other grounds*, 459 U.S. 375 (1983) 11, 13, 14

O'Neil v. Appel, 165 F.R.D. 479 (W.D. Mich. 1996) 20

Sharp v. Coopers & Lybrand, 649 F.2d 175 (3rd Cir. 1981), *cert. denied*, 455 U.S. 938 (1982) 13

Six Mexican Workers v. Arizona Citrus Growers, 904 F.2d 1301 (9th Cir. 1990) 21

Ticor Title Ins. Co. v. Brown, 511 U.S. 117 (1994) 15

Vervaecke v. Chiles Heider & Co., Inc., 578 F.2d 713 (8th Cir. 1978) 11

Wilson v. Comtech Telecommunications Corp., 648 F.2d 88 (2d Cir. 1981) 9

Statute:

15 U.S.C. § 77j(b) 7, 22, 25

Cited Authorities

Page

Rules:

Federal Rule of Civil Procedure 23 ..... 23, 24, 25

United States Supreme Court Rule 14.3 3

United States Supreme Court Rule 15.2 2

Other Authorities:

17 C.F.R. § 240.10b-5 ..... 1, 2, 7, 15, 22, 25

4 Bromberg & Lowenfels, *Securities Fraud and Commodities Fraud* § 8.6 (1988) 19

PRELIMINARY STATEMENT

Contrary to petitioner's arguments, the majority opinion of the Ninth Circuit Court of Appeals in *Binder v. Gillespie*, Order and Opinion dated July 26, 1999 (Appendix ("App.") A) (the "Binder Decision"), does not conflict with Supreme Court precedent.[1] The Binder Decision, moreover, does not raise questions of national importance, and certainly does not "affect the substantial number of Rule 10b-5 securities and other class action cases processed by the courts each year, the efficient system-wide administration of such cases and continued implementation of the anti-fraud purposes and objectives of the federal securities laws." Petition for Writ of Certiorari ("Petition") at 16. The Binder Decision also does not conflict with the decisions of other Circuit Courts. Rather, the Binder Decision represents the application of well-developed legal principles to the indisputable facts in a single case. Therefore, the Binder Decision does not warrant review by this Court.

The Ninth Circuit thoroughly examined the relevant legal authority, reviewed the undisputed evidence, and then affirmed the district court's conclusions that: (1) the *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 153 (1972), presumption of reliance, "involving primarily a failure to disclose," is not applicable *in this case*; (2) petitioner failed to meet his burden of adducing facts to rebut the showing that the "over-the-counter" ("OTC") market for the stock of Aqua Vie Beverage Corporation ("AVBC" or "the Company"), the "pink sheet" security at issue in this lawsuit, was not efficient; and (3) petitioner could not establish, as a matter of law, that respondents made

1. The opinion is reported at 184 F.3d 1059 (9th Cir. 1999).

any material misrepresentations or omissions that caused any losses for the putative class over the period when AVBC stock was traded on the Boston Stock Exchange ("BSE"). Petitioner offers no legitimate reason to disturb these well-founded conclusions.

Notwithstanding petitioner's argument that this case will affect a "substantial number" of Rule 10b-5 cases, no published decisions have cited the Binder Decision — much less suggested that the Binder Decision somehow calls for a result different than what follows from pre-existing caselaw. The Ninth Circuit panel that handed down the Binder Decision, moreover, entertained, and rejected, similar apocalyptic arguments made by petitioner here when it voted to deny his petition for a rehearing. Order and Opinion dated July 26, 1999 (App. A at 7a). Additionally, no active judge sitting on the Ninth Circuit voted to grant petitioner's request for rehearing *en banc*. Order and Opinion dated July 26, 1999 (App. A at 8a). Implicit in the Ninth Circuit's denial of rehearing and rehearing *en banc* is the recognition that the Binder Decision conflicts with *no* decision of the Supreme Court and involves *no* question of exceptional importance. Given this, respondent Deloitte & Touche LLP ("Deloitte") respectfully requests that the Supreme Court also deny the Petition for Writ of Certiorari.

STATEMENT OF THE CASE

I. Objection to Petition

Pursuant to Rule 15.2 of the Supreme Court Rules, Deloitte objects to the "factual" presentation found in petitioner's Statement of the Case. Petitioner's Statement of the Case includes the recitation of countless "facts" that have

absolutely no bearing on the issues presented to this Court, and that are unsupported by the record presented to the Ninth Circuit Court of Appeals. The inclusion of these irrelevant facts also appears to violate Rule 14.3 of the Supreme Court Rules, which requires the Petition to be "stated briefly and in plain terms." Given the presentation made by petitioner, Deloitte is constrained to present the following facts that are relevant to it and the issues presented to this Court. It has attempted to keep that presentation as brief as possible so as not to further burden the Court, but cannot leave petitioner's unsupported assertions unrebutted.

II. The Facts Pertinent to Deloitte

In the early 1990's the "new age" beverage market was taking off. AVBC sought to enter that market by developing and selling bottled noncarbonated, lightly flavored spring water. Before 1991, AVBC's predecessor operating company, KWC, Inc., was privately held. In January 1991, as the result of a merger, AVBC became a public company. During 1991, when petitioner purchased stock in AVBC, and through most of 1993, AVBC's stock was traded on the OTC market. Sometime after December 1, 1993, trading of the Company's common stock commenced on the BSE.

AVBC's product never achieved any significant market success. As reported in the audited financial statements issued during the putative class period, AVBC had less than $240,000 in sales during 1991, and only approximately $1.3 million in sales during 1992. It operated at a reported loss every year. Further, it reported a negative net worth, which was in excess of $5,000 in 1991 and over $1.5 million in 1992.

Deloitte was first engaged in the summer of 1991 to audit AVBC's (KWC Inc.'s) 1990 financial statements. The 1990 financial statements were publicly disseminated for the first time on October 22, 1991, when they were included in an amendment to a Form 8 filed with the SEC. Thereafter, during the putative class period, Deloitte audited the annual financial statements of AVBC for the years ended December 31, 1991 and 1992. The audited 1993 financial statements were completed after the end of the putative class period.

The engagement letters executed by AVBC delineated the services to be performed by Deloitte. As stated by Jeff Stengel, the Deloitte manager in charge of the AVBC 1991 audit and the partner in charge of the 1992 and 1993 audits, Deloitte "never reviewed or had a business relationship with [AVBC] that we were engaged to review their 10-Q's." Deloitte did not review any unaudited or interim AVBC financial statements. AVBC financial projections, including those that appeared in the Management's Discussion and Analysis ("MD&A") section of the Company's 10-Q's, were prepared solely by AVBC personnel.

AVBC was a development stage enterprise as defined by Generally Accepted Accounting Principles from its inception in November 1989 through mid-1992; that is, AVBC had not reached its planned level of operations (the principal operations of the Company had either not commenced or not generated significant revenue), and was devoting most of its efforts to activities which included product research and development, establishing sources of supply, developing product markets and starting up production.

Deloitte's audit reports for the years ending December 31, 1990 and 1991 emphasized the uncertainties facing AVBC:

> The Company is in the development stage at December 31, . . . Recovery of the Company's assets is dependent upon future events, the outcome of which is indeterminable. In addition, successful completion of the Company's development program and its ultimate attainment of profitable operations is dependent upon obtaining adequate financing to fulfill its development activities and achieving a level of sales adequate to support the Company's cost structure.

By the end of 1992, although AVBC began to move beyond classification as a development stage enterprise, the Company continued to face vast financial uncertainties. Accordingly, the audit report and notes to the financial statements for the year ended December 31, 1992, emphasized Deloitte's conclusion that substantial doubt existed about AVBC's ability to continue as a going concern for a reasonable period. On this issue, the report stated:

> The accompanying financial statements . . . have been prepared assuming that the Company will continue as a going concern. . . . [T]he Company's recurring losses from operations, net stockholders' capital deficiency and negative operating cash flow raise substantial doubt about its ability to continue as a going concern.

Thus, not only did AVBC's financial statements disclose that the Company had no net earnings and no net worth, but,

in addition, Deloitte directly advised all readers of its report: (a) that future events, the outcome of which could not be predicted, would determine whether the Company would survive, and (b) that unless AVBC obtained adequate financing in the future and achieved a level of sales adequate to support its cost structure, it would not succeed.

Applying "an asset and income approach" to valuation, and relying on information contained in the financial statements at issue in the lawsuit[2], petitioner's valuation expert, Dennis R. Reinstein, concluded that AVBC and its common stock had *no* value. This confirms the conclusion of petitioner's damages expert, Dr. John Hekman, that the market value of AVBC stock was not based on current levels of Company assets, sales or earnings.

Also relying on financial statements audited by Deloitte, Wright, Houlihan and Associates, Inc. ("Wright, Houlihan"), an independent valuation company retained by the Company, concluded that as of October 1, 1992, AVBC and its stock had only negligible value. Wright, Houlihan wrote that "[b]ecause the Company has current operating losses and a history of losses, and negative net worth, public market multipliers based on earnings or book value are meaningless." Wright, Houlihan first determined that the gross market value of the Company was $2.8 million, and then derived a value for its stock, as of October 1, 1992, of $0.094 per share (applying a blockage discount to the large block of restricted stock being valued). Yet, in October 1992,

2. Specifically, the Deloitte-audited balance sheets of AVBC for the years ended 1992 and 1993; the Deloitte-audited AVBC statement of operations for the years ended 1991, 1992 and 1993; and the Deloitte-audited AVBC statements of cash flows for the years ended 1991, 1992 and 1993.

the quoted bid price for AVBC stock was approximately $2.50 per share. Thus, it is apparent that petitioner's expert, Dr. Hekman, was correct in concluding that "virtually all of the market value of AVBC stock during the Class Period was . . . *not* [due] to the current levels of sales, assets or earnings of the Company."

Petitioner purchased AVBC stock in September 1991, before any Deloitte-audited financial statement was issued. The complaint, brought against AVBC and certain of its former officers and directors, as well as Deloitte, alleges a number of claimed misrepresentations, including, particularly, publication by AVBC of allegedly false sales projections. As stated above, Deloitte played no role in the preparation or dissemination of those projections. Nevertheless, petitioner alleged that Deloitte violated Section 10(b) of the Securities and Exchange Act of 1934 (15 U.S.C. § 77j(b)) ("§ 10b") and Rule 10b-5 (17 C.F.R. § 240.10b-5) ("Rule 10b-5").

After reviewing the record presented to it, the district court ruled that the claims of the putative class who bought AVBC stock between August 1, 1991 and February 28, 1994 (the "Class Period") must be dismissed because the class could not satisfy all the elements under § 10(b) and Rule 10b-5. The district court determined that the class would have to satisfy the reliance element of its securities-fraud claim through a presumption, otherwise individual questions of reliance would predominate over questions common to the class. The district court ruled, however, that no presumption was available to the class. Because the action was not primarily an omissions case, involving the omission of material facts by the respondents, the class was not entitled to the *Affiliated Ute* presumption of reliance. The district

court also ruled that the class was not eligible for the fraud-on-the-market presumption because petitioner had not met his burden of establishing that the market for AVBC stock, which traded on the OTC market until December 1993, was efficient. The district court, therefore, decertified the class through December 1993.

The district court noted that the class might qualify for the fraud-on-the-market presumption during the period when AVBC stock traded over the BSE, from December, 1993 through February 28, 1994. The district court, however, decertified the class because petitioner could not establish that respondents issued any false statements or omissions during this period that caused any investor loss. After decertifying the class, the district court declined to exercise supplemental jurisdiction and, therefore, dismissed the state class claims. The district court then granted summary judgment on petitioner's individual federal and state claims in Deloitte's favor because his evidence was insufficient to implicate Deloitte's participation in any scheme to defraud him in connection with his purchase of AVBC securities. A majority of the Ninth Circuit panel hearing this case on appeal affirmed all of the district court's conclusions.

REASONS FOR DENYING THE WRIT

I. The Ninth Circuit Correctly Concluded That A Presumption Of Reliance Does Not Apply in This Case.

The Ninth Circuit affirmed the district court order granting summary judgment in Deloitte's favor and decertifying the plaintiff class because petitioner could not establish two essential elements of his case: reliance and

causation. To prevail on a securities fraud claim, petitioner was required to prove that: (1) Deloitte made misrepresentations or omissions; (2) the purported misrepresentations or omissions were material; (3) Deloitte acted with scienter; (4) petitioner relied on the purported misrepresentations or omissions; and (5) petitioner was damaged as a result of the purported misrepresentations or omissions. *Basic v. Levinson*, 485 U.S. 224 (1988). Specifically, with regard to the element of reliance, both the Ninth Circuit and the district court held that the putative plaintiff class was not entitled to invoke a presumption of reliance. Order and Opinion dated July 26, 1999 (App. A at 14a, 15a and 17a).

In the context of federal securities cases, this Court has allowed a presumption of reliance in two very limited circumstances, both of which present peculiarly difficult evidentiary burdens for a plaintiff seeking to establish reliance. In *Affiliated Ute,* a case that involved the failure to disclose material information during face to face meetings, this Court held that positive proof of reliance is not a prerequisite to recovery in cases involving "primarily a failure to disclose." 406 U.S. at 153. This Court adopted the presumption of reliance in cases involving primarily omissions because "[u]nlike instances of affirmative misrepresentation where it can be demonstrated that the injured party relied upon affirmative statements, in instances of total nondisclosure, as in *Affiliated Ute*, it is of course impossible to demonstrate reliance." *Wilson v. Comtech Telecommunications Corp.*, 648 F.2d 88, 93 (2d Cir. 1981); *see also Basic,* 485 U.S. at 245; *Blackie v. Barrack*, 524 F.2d 891, 908 (9th Cir. 1975), *cert. denied*, 429 U.S. 816 (1976). Omission cases involve what has been characterized as "a speculative negative (I would not have bought had I known)." *Blackie, id.* A presumption of reliance is

unnecessary and inappropriate in misrepresentation cases because a plaintiff can identify the alleged misrepresentations and demonstrate how each misrepresentation induced him or her to act.[3]

In *Basic*, this Court adopted a presumption of reliance in the form of the fraud-on-the-market doctrine. That doctrine is "based on the hypothesis that, in an open and developed securities market, the price of a company's stock is determined by the available material information regarding the company and its business." *Basic*, 485 U.S. at 241. This Court adopted the fraud-on-the-market doctrine because it provided an appropriate (but rebuttable) link between the dissemination of information into the market and a decision to purchase or sell based on market price. This Court made it clear, however, that the fraud-on-the-market doctrine applies *only* if the market for the particular security at issue is efficient — that is, so "open and developed" that the price of the security reflects all available public information about the economy, about financial markets, and about the specific company involved. *Basic*, 485 U.S. at 248, n.27. If the security at issue trades in an inefficient market, the presumption does not apply.

Contrary to petitioner's argument, in its Binder Decision, the Ninth Circuit did not issue any precedent-shattering pronouncements concerning either the *Affiliated Ute* presumption of reliance or the fraud-on-the-market doctrine. The Ninth Circuit simply examined all the uncontroverted evidence presented to it and then determined that neither the *Affiliated Ute* presumption nor the fraud-on-the-market doctrine applied in this case.

---

3. This is the complete answer to the argument in Judge Reinhardt's dissent on which petitioner places so much reliance in his presentation to this Court. *See, e.g.* Petition at 18-20.

II. The Ninth Circuit Correctly Held That This Case Does Not Primarily Involve Omissions And, Therefore, the *Affiliated Ute* Presumption Does Not Apply

The Ninth Circuit concluded that the putative class was not entitled to invoke the presumption of reliance articulated in *Affiliated Ute* because this case does not primarily involve omissions. The substance of petitioner's claim against Deloitte is that the financial statements audited by Deloitte were allegedly false and misleading.[4] *See* First Amended Class Action Complaint filed December 10, 1996 (App. C at 43c, & 29(16); 50c, & 29(34); 53c, & 29(41)). In reaching the determination that petitioner's case did not primarily involve omissions, both the Ninth Circuit and the district court carefully analyzed the allegations of the complaint and reached the same conclusion: "Binder's complaint contains both allegations of omissions and misrepresentations, and at the very least, must be characterized, as the district court noted, as a 'mixed case of misstatements and omissions.' " Order and Opinion dated July 26, 1999 (App. A at 12a).

4. Indeed, the fact that petitioner's allegations against Deloitte relate to written financial statements is sufficient to dispose of his *Affiliated Ute* argument as to Deloitte because federal courts generally have held that cases involving "misstatement[s] and omission[s] within the four corners" of a financial or disclosure document do not implicate the *Affiliated Ute* presumption of reliance. *Vervaecke v. Chiles Heider & Co., Inc.*, 578 F.2d 713, 718 (8th Cir. 1978). *See also Huddleston v. Herman & MacLean*, 640 F.2d 534, 548 (1981), *aff'd in part and rev'd in part on other grounds*, 459 U.S. 375 (1983) ("[t]his case, involving alleged misstatements and omissions in a prospectus published pursuant to a public offering, cannot properly be characterized as an omissions case of the type for which the *Affiliated Ute* presumption was fashioned."). Significantly, the petition does not address this issue.

Consistent with Supreme Court precedent, a majority of the Ninth Circuit panel then concluded that in such a mixed case, petitioner could not invoke the *Affiliated Ute* presumption of reliance because the case could *not* be analytically characterized as one that primarily alleges omissions. Order and Opinion dated July 26, 1999 (App. A at 14a).

III. The Binder Decision Presents No Questions of National Importance That The Supreme Court Must Settle

The Ninth Circuit's conclusion that the *Affiliated Ute* presumption did not apply to the case before it is a well-reasoned decision that was directly based on Supreme Court precedent. Given that the Binder Decision does not conflict with any prior decisions of this Court, no questions of national importance are implicated. Simply put, the Binder Decision does not warrant an examination into federal substantive and procedural law by this Court, as petitioner claims. Petition at 16.

Not only does the Binder Decision not conflict with Supreme Court precedent, but it also does not conflict with the decisions of other Circuit Courts that have addressed the *Affiliated Ute* presumption of reliance. The fact that petitioner identifies absolutely no conflict among the Circuit Courts also supports the conclusion that this case does not warrant the intervention of the United States Supreme Court. In fact, petitioner ignores the degree of harmony that exists among the decisions of the Circuit Courts.

Affiliated Ute's holding that a presumption of reliance applies only in cases that involve primarily omissions has been consistently followed by all Circuit Courts. Only a few

Circuit Courts, moreover, have even addressed the issue of whether the *Affiliated Ute* presumption applies in so-called mixed cases. Of the Circuit Courts that have addressed this issue, all are in agreement with regard to the appropriate approach: a court must first analyze the facts of each particular case to determine if the case involves misrepresentations or omissions. Then, the court must determine if the *Affiliated Ute* presumption applies. *See Huddleston v. Herman & MacLean*, 640 F.2d at 548; *Finkel v. Docutel/Olivetti Corporation*, 817 F.2d 356, 359 (5th Cir. 1987), *cert. denied*, 485 U.S. 959 (1988); *Cavalier Carpets, Inc. v. Caylor*, 746 F.2d 749, 756 (11th Cir. 1984); *Sharp v. Coopers & Lybrand*, 649 F.2d 175, 188 (3rd Cir. 1981), *cert. denied*, 455 U.S. 938 (1982). The mere fact that each of these courts concluded that it had to determine first whether the case involved omissions *or* misrepresentations carries with it the understanding that under *Affiliated Ute*, omissions and misrepresentations are to be treated differently.

With regard to the conclusions reached by the Circuit Courts that have addressed the issue of whether the *Affiliated Ute* presumption applies in mixed cases, again, no conflict exists. In fact, all but one Circuit Court has expressly determined that the *Affiliated Ute* presumption does *not* apply in a mixed case.[5] For example, in *Huddleston v. Herman &*

5. *See Sharp v. Coopers & Lybrand, supra*. In *Sharp v. Coopers & Lybrand*, however, the Third Circuit recognized that the *Affiliated Ute* presumption generally applies to omissions. 649 F.2d at 187. Additionally, the Third Circuit declined to issue any sweeping pronouncement concerning the *Affiliated Ute* presumption and its application to mixed cases. 649 F.2d at 189, n.19. Rather, the Third Circuit held that in the particular circumstances of the case before it, which involved the appropriate jury instruction based on the (Cont'd)

MacLean, the leading "mixed case," the Fifth Circuit Court of Appeals held that "[A mixed] case is not a case in which the difficulties of proof of reliance require the application of the *Affiliated Ute* presumption." 640 F.2d at 548. The Eleventh Circuit in *Cavalier Carpets, Inc. v. Caylor* agreed with the *Huddleston* analysis and held: "We adhere to the mixed case rule of *Huddleston, supra*, and find that the jury was correctly instructed that it must find plaintiffs relied upon the misstatements and omissions for plaintiffs to recover." 746 F.2d at 757.

Another factor that undermines petitioner's argument of "material importance" is that *Huddleston*, which expressly addressed the issue of whether *Affiliated Ute* applies in mixed cases, has been considered by this Court. *Huddleston*, 640 F.2d at 548, *aff'd in part and rev'd in part on other grounds*, 459 U.S. 375 (1983). This Court's affirmance of much of the Fifth Circuit's decision in *Huddleston* supports the conclusion that this Court intended the presumption created in *Affiliated Ute* to be available only in cases involving primarily a failure to disclose. *Huddleston*, 640 F.2d at 548. That conclusion is buttressed by this Court's denial of the petition for writ of certiorari in *Finkel v. Docutel/Olivetti Corp., supra*.

In *Finkel*, the Fifth Circuit discussed *Affiliated Ute* at considerable length and concluded that in light of this Court's decision in that case, a trial court must "analytically

---

(Cont'd)
specific allegations against the defendants in that case, the district court correctly allocated the burden of proof on the issue of reliance. The Third Circuit most certainly did not hold that the *Affiliated Ute* presumption applies to all mixed cases, much less to cases like the one before this Court, which does not primarily involve omissions.

characterize a 10b-5 action as either primarily a nondisclosure case (which would make the presumption applicable), or a positive misrepresentation case." 817 F.2d 359. That, of course, is what the trial court did in this case, as the Ninth Circuit expressly observed. Order and Opinion dated July 26, 1999 (App. A at 13a-14a).[6] Just as there was no reason to grant certiorari in *Finkel* to review that analytic approach, none exists here.

IV. *Basic* Did Not Alter the *Affiliated Ute* Presumption

Petitioner argues that *Basic* altered the *Affiliated Ute* presumption by eliminating the requirement that a case must involve primarily omissions before the presumption of reliance may be invoked. Petition at 20. *Basic* did no such thing. *Basic* had nothing to do with the *Affiliated Ute* presumption of reliance, but, rather, whether this Court would recognize a presumption of reliance based on the fraud-on-the-market doctrine. In recognizing such a presumption, this Court cited *Affiliated Ute* merely to illustrate another circumstance in which the Court had permitted the invocation of a presumption of reliance. *Basic*, 485 U.S. at 243. Significantly, so as to leave no confusion about the point it was making concerning its earlier holding, in *Basic*, this Court immediately and explicitly cited to pages 153 and 154 of the *Affiliated Ute* decision. There, this Court stated

6. Stripped of all its claims of implicating questions of national importance, petitioner's argument boils down to the fact that he believes the Ninth Circuit erred in reaching its conclusion that the *Affiliated Ute* presumption did not apply in this case. That, however, is not a proper reason for seeking certiorari, as this Court has ruled that it will not grant certiorari simply to correct an error in a court of appeals decision. *Ticor Title Ins. Co. v. Brown*, 511 U.S. 117, 122 (1994). In any event, the Ninth Circuit's conclusion is amply supported by the record and contains no error.

unequivocally that "[u]nder the circumstances of this case, involving primarily a failure to disclose, positive proof of reliance is not a prerequisite to recovery." *Affiliated Ute*, 406 U.S. at 153-154, directly cited by the Court in *Basic* at 485 U.S. at 243. Given the clear language in *Affiliated Ute* and the express citation to that language in *Basic*, petitioner cannot seriously claim that *Basic* altered the holding in *Affiliated Ute*.

Furthermore, contrary to petitioner's misreading of case law, *Affiliated Ute* was not a "mixed case." Petition at 17, fn. 3. In *Affiliated Ute*, this Court observed that the central feature of the defendants' fraud was to "stand mute" while facilitating the transfer of the plaintiffs' stock to third parties for less than full value. *Affiliated Ute*, 406 U.S. at 153. While the defendants did make some affirmative misstatements, those statements were few in number and clearly incidental to the underlying scheme to "stand mute." *Affiliated Ute*, 406 U.S. at 152, 153. This explains why this Court characterized the case as one involving "primarily a failure to disclose." *Affiliated Ute*, 406 U.S. at 153.

V. The Ninth Circuit Correctly Concluded That the Putative Class Could Not Invoke a Presumption of Reliance on the OTC Market for AVBC Stock

The Binder Decision also does not make precedent-shattering pronouncements concerning the fraud-on-the-market theory. The Binder Decision simply reflects the fact that petitioner was unable to meet his burden of presenting facts to establish that the OTC market for AVBC stock was efficient, a necessary precondition to invocation of the fraud-on-the-market presumption of reliance. As such, the Binder Decision does not conflict with *Basic*.

Petitioner offers the strained argument that the Binder Decision conflicts with *Basic* because it "develops" a test to determine the efficiency of a market, which *Basic* does not do. Petition at 26, fn. 10. Additionally, without citing any case law to support his point, petitioner argues that the test for determining whether the fraud-on-the-market doctrine applies is not whether the security at issue trades in an open and efficient matter, but if "information regarding the security and the issuer is available to participants in the trading market for such security." Petition at 25. The holding of *Basic* establishes that petitioner is wrong on both points.

The fraud-on-the-market doctrine was adopted because of the evidentiary problems that securities class action plaintiffs face in proving that when they purchased or sold a security they relied on a particular statement that affected the price of that security. In *Basic*, this Court, affirming a Sixth Circuit decision, held

> that in order to invoke the presumption of reliance [under the fraud-on-the-market doctrine], a plaintiff must allege and prove: (1) that the defendant made public misrepresentations; (2) that the misrepresentations were material; (3) *that the shares were traded on an efficient market*; (4) that the misrepresentations would induce a reasonable, relying investor to misjudge the value of the shares; and (5) that the plaintiff traded the shares between the time the misrepresentations were made and the time the truth was revealed.

Basic, 485 U.S. at 248, n.27 (emphasis added). This Court added that the second and fourth parts of the test could be collapsed into one. *Basic*, *id.* This Court said nothing about

eliminating the efficient market requirement. Therefore, petitioner is in error to the extent he suggests that the concept of an efficient market is not central to the *Basic* Court's analysis.

Additionally, the Binder Decision is not at odds with *Basic* because it "developed" a test to determine if a security traded in an efficient market. While it is true that this Court has not adopted a specific test to determine if the market for a particular stock is efficient, its decision in *Basic* provides more guidance than petitioner acknowledges. This Court spoke of an "open" market, a "developed" market, and a market in which the prices of the security reflect all available public information about the economy, about financial markets, and about the specific company involved. *Basic*, 485 U.S. at 248, n.27.

In determining whether the market for AVBC stock traded in an efficient market, which would trigger the fraud-on-the-market doctrine and its presumption of reliance, the Ninth Circuit applied the indicia of efficiency that were set forth in *Cammer v. Bloom*, 711 F. Supp. 1264 (D.N.J. 1989). The *Cammer* decision simply analyzes and applies indicia of "open" and "developed" markets, and markets that reflect new information about a company in the price of that company's stock. As the Binder Decision correctly observed, the "*Cammer* factors are designed to help make the central determination of efficiency in a particular market." Order and Opinion dated July 26, 1999 (App. A at 16a-17a). They amplify *Basic*; they do not conflict with it. That is why so many other courts have applied the *Cammer* factors in their own analyses. *See* Order and Opinion dated July 26, 1999 (App. A at 15a-16a). The fact that the Ninth Circuit used the *Cammer* factors to analyze whether the market at issue was

efficient does not place the Binder Decision in conflict with *Basic*. The Ninth Circuit merely emphasized that for the *Basic* presumption to apply, a stock must be traded in an efficient market.

VI. Petitioner Failed to Establish a Genuine Issue of Fact with Respect to the Demonstrated Inefficiency of the OTC Market for AVBC Stock

The undisputed evidence established that AVBC stock was traded on the OTC market through "pink sheets" from at least the beginning of the putative class period (August 1, 1991) to December 1993. The "pink sheets" are daily listings of "bid" and "ask" quotes that do not necessarily reflect any actual trading and do not reflect the trading volume of any particular stock. The stocks quoted by dealers in the "pink sheets" (or, since approximately June 1990, on NASDAQ's computerized bulletin board) are on the lowest rung of the OTC market.

Whether or not the evidence in this case is examined under the *Cammer* test for efficiency, numerous key facts support the conclusion that the market for AVBC was not efficient. First, the trading volume of AVBC was not reported publicly. Therefore, for virtually the entire class period, important trading information for AVBC stock was not widely available, as required for a developed market. *See* 4 Bromberg & Lowenfels, *Securities Fraud and Commodities Fraud* at § 8.6 (1988).

Second, no evidence exists that suggests that any securities analysts followed AVBC or reported on the stock during the class period.

Third, while petitioner offered an expert who claimed through unsupported testimony that there were a "substantial number of market makers" during the would-be class period, he provided no competent evidence regarding such claimed market makers. In any event, "the mere number of market makers, without much more information, is . . . virtually meaningless." *O'Neil v. Appel*, 165 F.R.D. 479, 501-502 (W.D. Mich. 1996).

Fourth, AVBC has never been eligible to file an SEC Form S-3. The SEC allows companies to file the "abbreviated" S-3 form "only on the premise that the stock is already traded on an open and efficient market, such that further disclosure is unnecessary." *O'Neil*, 165 F.R.D. at 502. AVBC's ineligibility to file this form weighs strongly against the efficiency of the market for AVBC stock.

Instead of focusing on these facts, petitioner simply asserts that all securities trading on the OTC market "should be *deemed* to be trading in an 'efficient market.' " Petition at 27; emphasis added. In other words, petitioner seeks yet another presumption — indeed, an irrefutable presumption — regarding market efficiency, directly contrary to this Court's holding in *Basic* that "a plaintiff must allege *and prove* . . . that the shares were traded on an efficient market." 458 U.S. at 248, n. 27; emphasis added. Petitioner's argument also avoids the real issue, that is, whether the *market for AVBC stock* was efficient. With no evidence in the record to support any indicia of efficiency, as well as no competent or admissible expert testimony,[7] the Ninth Circuit correctly

7. The panel unanimously affirmed the district court's evidentiary rulings striking certain of the "expert" testimony that petitioner still seeks to urge on this Court. Order and Opinion dated (Cont'd)

concluded that petitioner did not meet his burden of establishing genuine issues of material fact as to whether the market for AVBC stock was efficient. Therefore, the putative class was not entitled to invoke a presumption of reliance on an efficient market.[8]

VII. The Record Established That Deloitte's Alleged Misrepresentations and Omissions Did Not Cause Petitioner's Loss

The Ninth Circuit properly held that petitioner failed to adduce evidence sufficient to raise a triable issue that any allegedly material misrepresentations made during the time that AVBC stock traded on the BSE caused any investor loss. Deloitte audited and reported on historical financial information. Petitioner's own expert asserted that the market value of AVBC's stock did not result from such reported historical financial information but, instead, from expectations of investors as to AVBC's future prospects.

(Cont'd)
July 26, 1999 (App. A at 22a-23a). By contrast, Deloitte offered competent evidence in the form of affidavits from its experts to show that there was no statistically significant movement of AVBC stock caused by news of corporate events or financial releases.

8. Petitioner tries to reargue the Circuit's affirmance of the district court's order decertifying the class after it concluded that no presumptions of reliance were available. Petition at 9-12. But, he does not argue that the district court abused its discretion in so ruling. Yet, that is the question on appeal. *See Six Mexican Workers v. Arizona Citrus Growers*, 904 F.2d 1301, 1304 (9th Cir. 1990). Instead, he asserts that the panel misread *Basic*. However, *Basic* plainly states that individual issues predominate when each putative class member must prove individual reliance. *Basic*, 485 U.S. at 242. Supreme Court review on this issue plainly is unwarranted.

Indeed, he determined that AVBC stock had a value of zero based on the very financial statements audited by Deloitte. Consequently, petitioner's expert concluded that "the current levels of sales, assets or earnings of the Company" were not causal factors inflating "the market value of AVBC's stock during the Class Period."

Given the uncontested fact that the historical financial statements Deloitte audited or allegedly commented on had no effect on the market value of AVBC stock, petitioner could not present a triable issue relating to his burden of proving that "the [alleged] misrepresentations and omissions . . . impacted the value of the investment." Entry of summary judgment for Deloitte, therefore, was warranted.

VIII. The Decision to Decertify the Class Does Not Conflict With Supreme Court Precedent

Petitioner argues that the Ninth Circuit decertified the class and dismissed the class Rule 10b-5 claims "solely on the basis that [petitioner] could not maintain individual claims against all of the same defendants because he could not satisfy the purchaser or seller requirement as to all of such defendants. . . ." Petition at 28. Petitioner's argument is wrong and misstates the holding of the Ninth Circuit.

The Ninth Circuit's decision to affirm the district court's dismissal of the class claims was not "solely on the basis that [petitioner] could not maintain individual claims." The Ninth Circuit affirmed the district court's decision to dismiss the claims of the putative class who bought AVBC stock during the Class Period because the class could not satisfy all the elements under § 10(b) and Rule 10b-5. As noted above, both the Ninth Circuit and the district court

determined that the class would have to satisfy the reliance element of its securities-fraud claim through a presumption, otherwise individual questions of reliance would predominate over questions common to the class. The Ninth Circuit, however, affirmed the district court decision that no presumption was available to the class because this action was not primarily an omissions case and petitioner had not met his burden of establishing that the market for AVBC stock was efficient. Order and Opinion dated July 26, 1999 (App. A at 14a and 17a). Given this, the Ninth Circuit affirmed the district court's decision to decertify the class through December, 1993. Order and Opinion dated July 26, 1999 (App. A at 17a).

The Ninth Circuit then affirmed the district court's decision to decertify the class from December, 1993 through February 28, 1994 (the end of the Class Period) because petitioner could not establish that Deloitte issued any false statements or omissions during this period that caused any investor loss. Order and Opinion dated July 26, 1999 (App. A at 19a). Only after going through this rigorous analysis did the Ninth Circuit affirm the district court's decision to grant summary judgment on petitioner's individual federal and state claims in Deloitte's favor because his evidence was insufficient to implicate Deloitte's participation in any scheme to defraud him in connection with his purchase of AVBC securities. Order and Opinion dated July 26, 1999 (App. A at 22a).

Petitioner also argues that the Ninth Circuit's decision to affirm the district court's decertification of the putative class conflicts with Supreme Court precedent that interprets and applies Rule 23 of the Federal Rules of Civil Procedure. Petition at 17. Specifically, petitioner claims that the Binder

Decision conflicts with *General Telephone Co. of Southwest v. Falcon*, 457 U.S. 147 (1982), which purportedly stands for the proposition that a Rule 23 class representative need not possess the same claims against all the same defendants as all members of the proposed class so long as common issues of law and fact predominate. Petition at 27. Not only does the decision to decertify the class not conflict with *General Telephone*, but petitioner is also wrong in his analysis of *General Telephone*. In fact, *General Telephone* actually supports the district court's decision to decertify the class.

In *General Telephone*, this Court vacated a district court's decision, which had been affirmed by the circuit court, to certify a class because the plaintiff did establish the existence of common questions of law or fact that were common to claims of the plaintiff and the class. This Court ruled that the district court erred because it presumed the existence of common questions of law and fact and failed "to evaluate carefully the legitimacy of [the] named plaintiff's plea that he was a proper class representative." *Id.* The Court added that a proposed class representative must not only prove the validity of an individual claim, but must also establish the existence of common questions of law or fact. *General Telephone*, 457 U.S. at 158. The Court said nothing about a Rule 23 class representative not needing to possess the same claims against all the same defendants as other class members so long as common issues of law and fact predominate.

Here, the Ninth Circuit properly affirmed the district court's decision to decertify the class. As this Court instructed in *General Telephone*, the district court evaluated the legitimacy of petitioner's claim that he was a proper class

representative and refused to presume the requirements of Rule 23. The district court examined all the evidence and determined: (1) the class should be decertified for the period when AVBC stock was trading on the OTC market because petitioner could not establish the reliance element of his § 10b and Rule 10b-5 causes of action; and (2) the class should be decertified for the period when AVBC stock was trading on the BSE because petitioner could not identify any statements or omissions that could have caused any investor loss. Although the district court had previously certified the class, decertification was proper because even "after the class certification order is entered, the judge remains free to modify it in light of subsequent developments in the litigation." *General Telephone*, 457 U.S. at 160.

With regard to the district court's decision to decertify the class for the period when AVBC stock was trading on the BSE, the district court determined that petitioner could not even establish the validity of his individual claim, as is required under *General Telephone*. Given this, it would have been improper for the district court to "presume that [petitioner's] claim was typical of other claims." *General Telephone*, 457 U.S. at 158-159. Both the Ninth Circuit and the district court correctly determined that simply alleging violations of Rule 10b-5 does not mean that petitioner is an appropriate class representative. *See General Telephone*, 457 U.S. at 157 (quoting *East Texas Motor Freight System, Inc. v. Rodriguez*, 431 U.S. 395, 405-406 (1977) ("the 'mere fact that a complaint alleges racial or ethnic discrimination does not in itself ensure that the party who has brought the lawsuit will be an adequate representative' ").

CONCLUSION

For the reasons set forth above, the Court should deny the Petition for Writ of Certiorari.

Respectfully submitted,

LOIS D. THOMPSON
Counsel of Record
DONALD S. URRABAZO
PROSKAUER ROSE LLP
Attorneys for Respondent
Deloitte & Touche LLP
2049 Century Park East
Los Angeles, CA 90067
(310) 557-2900